Nos. 15,256 and 15,257

United States Court of Appeals

For the Ninth Circuit

MARGURERITE FERRANDO and FRED FERRANDO, co-executors of the Last Will and Testament of Mario Ferrando, deceased; EDWARD FERRARI and GEORGE FERRARI, co-executors of the Last Will and Testament of Luigi Ferrari, deceased,

Appellants,

vs.

UNITED STATES OF AMERICA,

Appellee.

BRIEF OF APPELLANTS.

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STATEMENT OF JURISDICTION.

This is an appeal from final judgments of the United States District Court for the Northern District of California, Southern Division, The Honorable Louis E. Goodman Presiding, entered on the 22nd day of June, 1956. The proceedings below were commenced with the filing on February 16, 1955, of complaints pursuant to Section 3772 of the Internal Revenue Code of 1939 for the recovery of penalties collected

by Appellee upon the alleged authority of Section 3612 (d)(1) of said Code from Appellants as co-executors of the Last Will and Testaments of the above named decedents.

Notice of this appeal was timely filed on July 19, 1956.

STATEMENT OF THE CASE.

Estate of Ferrari.

Appellants are the sons of Luigi Ferrari who died in San Francisco on August 2, 1946. His last will and testament was admitted to probate on August 30th of that year and on the same day Appellants were appointed co-executors of the will. Forthwith they employed as counsel for the estate Mr. Lloyd J. Cosgrove, a widely known and reputable attorney in their immediate community who, for many years prior to his death, had represented their father in legal matters. Mr. Cosgrove accepted the employment and the Appellants, as the record shows, did everything within their power to furnish him with the assistance and information he required for the task.

The federal estate tax return of the estate became due on November 2, 1947. This time was duly extended in writing in accordance with Treasury Department Regulation 105 until December 2, 1947. Prior to that time, Appellants signed a Federal Estate Tax Return in the office of Mr. Cosgrove. He explained that it was not necessary to pay the tax at that time, but that when it was paid, it would bear interest at the rate of six per cent (6%) per annum. (Tr. 181.)

Although the return was not complete, Mr. Cosgrove nevertheless, left it in the Office of the Deputy Collector of Internal Revenue at San Francisco, Mr. Paul Doyle. Subsequently, in the early part of 1948, Mr. Cosgrove employed the services of the accounting firm of Prior & McClellan to prepare a completed return and finally on April 22, 1949, the return left with Mr. Doyle was corrected by substituting various schedules, the completed return filed and the tax paid in full together with interest to the date of payment.

The Appellants did not know Mr. Paul Doyle and had no knowledge of a discussion or arrangement had by Mr. Cosgrove with him, nor were they aware that the filing of a complete return had been delayed or that possible penalties were involved until shortly before the final return was in fact filed. (Tr. 187-189.)

George and Edward Ferrari were born and raised in the Potrero and Mission Districts in San Francisco. George Ferrari completed High School and his brother, Edward, finished the first year of High School. Although their father and mother had, through great frugality, acquired a substantial amount of property by the time of the father's death, both of these Appellants have earned their livelihood by hard physical labor. Their business consists of buying vegetables in the wholesale market in San Francisco and personally delivering them to the restaurant trade in the city. All of the manual labor involved in the enterprise was carried on by the father, this decedent, and his three sons. A year before the death of Luigi

Ferrari his son, Anthony, died and after the death of Luigi in 1946, the entire burden of the business fell upon the shoulders of these Appellants. As the testimony indicates, they go to work at 4:30 in the morning and their tasks are not completed until late afternoon. The properties which their father and mother acquired, and which their mother acquired through the estate of their father, are managed and operated by the real estate firm of Madison & Burke.

Prior to the death of Luigi Ferrari, neither of these Appellants had ever acted in the capacity of a co-executor nor had they any connection with the probate of estates of decedents. They were totally unfamiliar with the nature of these proceedings in all of their aspects.

Estate of Ferrando.

The Appellants, Marguerite Ferrando and Fred Ferrando, are the surviving spouse and son, respectfully, of Mario Ferrando who died in San Francisco, California on April 20, 1947. The last will and testament of the deceased was admitted to probate on May 13th of that year and on the same day Appellants were appointed co-executors of the will. Within a few days after the death of Mr. Ferrando, Appellants employed Lloyd Cosgrove as their attorney. As in the Ferrari case, Mr. Cosgrove had represented the deceased in legal matters for many years prior to his death and drew his last will and testament.

Mr. Cosgrove accepted the employment and undertook to do everything required to administer the estate

in probate, including specifically the preparation of estate and inheritance tax returns. (Tr. 36, 67.)

Mr. Cosgrove frequently called upon Appellants for the purpose of signing documents required in the administration of the estate, the marshalling of the assets, and the making of court appearances. According to the testimony of Mr. Cosgrove, Mr. Ferrando responded promptly to all his various requests for information and assistance.

The federal estate tax return involved here became due on July 20, 1948. Mr. Cosgrove did not communicate this fact to Appellants in this case, nor did he take any action to obtain an extension of time within which to file the return. However, on February 8, 1949, Mr. Cosgrove addressed a letter to Mr. Ferrando advising him that the federal estate tax return had been completed, asking that he and his mother come to his office to sign it, and requesting that he "give this matter your usual prompt attention". (Tr. 38, Plaintiffs' Exhibit No. 1.)

Mr. and Mrs. Ferrando responded promptly to this request and shortly after signed the return in the office of Mr. Cosgrove. On or about the 15th day of February, Mr. Cosgrove called Mr. Ferrando and asked that he make out a check in payment of the tax, and that he would arrange to have it picked up. The check stub shows that it was written on February 17, 1949, though the cancelled check shows a typewritten date of July 15, 1948. (Tr. 47, 49—Defendant's Exhibits A and B.) Except for the date, the check was in the handwriting of Mr. Ferrando. Mr. Fer-

rando had no recollection with reference to the omission of the date from the check, and testified that he first became aware of the fact that the date July 15, 1948 was inserted on the check at the time it was offered as an exhibit at the first trial of Mr. Doyle and Mr. Cosgrove.

The estate tax return of the Ferrando Estate was prepared by the Messrs. Prior and McClellan, a firm of Certified Public Accountants whom Mr. Cosgrove employed in the late fall of 1948. (Tr. 97.)

The substance of Mr. Cosgrove's testimony was that prior to the due date of the return (July 25, 1948) he telephoned Mr. Paul Doyle, the Chief Office Deputy Collector of Internal Revenue, and advised him that he would be unable to timely file the return because of the pressure of business and that in response, Mr. Doyle told him to bring the return as soon as time would permit, which Mr. Cosgrove regarded as an indefinite oral extension of time. (Tr. 73.)

Mr. and Mrs. Ferrando never knew Paul Doyle, nor of any arrangements made or conversations had with him by Mr. Cosgrove. They had no knowledge that the return was filed late or that penalties were involved until the Internal Revenue Agents called on them several years later in connection with the investigation of Mr. Cosgrove and Mr. Doyle. (Tr. 40.)

Mrs. Ferrando is an Italian woman who came to this county from Uruguay in 1900 at the age of twelve. She did not attend school beyond the eighth grade. Although she was named co-executor in the will, her son discharged the major share of their

duties in the administration of the estate, though she made all the appearances required and signed all documents when called upon to do so. (Tr. 62, 63.) Fred Ferrando went to Portola Grammar School and to Mission High School in San Francisco, although he did not complete high school. From an early age he worked in his father's concrete contracting business and carried it on after his death.

Neither Mrs. Ferrando nor her son had ever before acted in the capacity of an executor and both were totally unfamiliar with the probate of estates. These facts, together with the fact that they employed an experienced attorney to represent them, were expressly recognized by the Court below in its Opinion and Order for Judgment. (Tr. 17.)

The facts of the cases summarized above are essentially without contradiction in this record, nor do they differ with the undisputed facts before this Court a few years ago in the criminal proceeding involving Mr. Cosgrove and Mr. Doyle, No. 13,626.

The Commissioner of Internal Revenue asserted the penalties in dispute pursuant to Section 3612(d)(1) of the 1939 Internal Revenue Code for failure to timely file the Estate Tax return in question. This action was commenced upon the ground that Appellants were entitled to the benefits of the exception provided in the statute in cases where "*. . . the failure to file . . . was due to reasonable cause and not to wilful neglect . . .*"

Appellants contend that as a matter of law, upon the record presented, they are entitled to the relief prayed for below.

SPECIFICATIONS OF ERROR RELIED UPON.

Estate of Ferrari.

1. The United States District Court erred in making the following findings of fact:

(a) The Appellants made no attempt to determine if their attorney was acting with diligence in preparing and filing a federal estate tax return as required by law.

(b) That the Appellants made no attempt to determine whether a federal estate tax return had been filed.

(c) That the Appellants' conduct failed to discharge their duty to prepare and file a federal estate tax return.

(d) That the Appellants were guilty of wilful neglect in failing to determine whether their attorney was acting with diligence in the preparation and filing of a federal estate tax return.

(e) That the failure to file a federal estate tax return within the period prescribed by law was not due to reasonable cause as to the Appellants.

2. The United States District Court erred in respect of the following conclusions of law:

(a) That the Appellants' conduct failed to discharge their duty to prepare and file a federal estate tax return.

(b) That there was no reasonable cause on the part of appellants for failure to file a federal

estate tax return within the period prescribed by law.

(c) That the Appellants' failure to file a federal estate tax return within the period prescribed by law was due to Appellants' wilful neglect.

(d) That the penalties assessed by the Appellee against the Appellants were validly assessed pursuant to the provisions of Section 3612(d)(1) of the Internal Revenue Code of 1939.

(e) That the Appellee was properly entitled to judgment in this cause.

3. The United States District Court, in its Opinion and Order for Judgment, erred in the following respects:

(a) The Court's statement to the effect that the showing made by Appellants that the delinquent filing in question was not due to any neglect on their part, is wholly lacking in clarity and persuasiveness, is not sustained by the evidence in the case.

(b) The Court's statement, that the testimony of Appellants to the effect that before the due date of the return they in fact and in good faith signed a completed return, is so equivocal and lacking in forthrightness that it is unacceptable, and is not only inconsistent with the Court's own conclusions of law and findings of fact, but is wholly unjustified by the record in the case.

(c) The Court erred in its statement that the Appellants failed to sustain their burden of show-

ing that the delinquent filing is due to reasonable cause and not to wilful neglect, because said statement is not sustained by the evidence in the case.

Estate of Ferrando.

1. The United States District Court erred in making the following findings of fact:

(a) The plaintiffs made no attempt to become familiar with their duties and obligations as executors of the Estate of Mario Ferrando.

(b) That plaintiffs, as co-executors of the last will and testament of Mario Ferrando, made no attempt to determine whether the attorney employed by them was acting with due diligence in preparing the federal estate tax return.

(c) That plaintiffs' conduct failed to discharge the duty to prepare and file a federal estate tax return.

(d) That there was no reasonable cause for the failure of plaintiffs to file a federal estate tax return within the time prescribed by law.

(e) That the failure of plaintiffs to make and file a return within the time prescribed by law was due to willful neglect.

2. The United States District Court erred in respect of the following conclusions of law:

(a) That the plaintiffs' conduct failed to discharge the duty to prepare and file a federal estate tax return.

(b) That the failure to file a federal estate tax return within the time prescribed by law for the Estate of Mario Ferrando is due to plaintiffs' willful neglect.

(c) That there is no reasonable cause for the failure of plaintiffs to file a federal estate tax return within the period prescribed by law.

(e) That the defendant was properly entitled to judgment in this cause.

3. The United States District Court erred in its Opinion and Order for Judgment in its conclusion that on the evidence in the case, with particular reference to the Court's asknowledgment of the facts that the plaintiffs were wholly unfamiliar with the administration of estates and employed an experienced attorney to represent them, that as a matter of law they nevertheless failed to discharge their duty of reasonable care in the circumstances.

ARGUMENT.

1. SUMMARY OF ARGUMENT.

(a) The statute under which the penalties in question were assessed and collected is Section 3612 (d) (1) of the Internal Revenue Code of 1939, which so far as applicable reads as follows:

"(d) Additions to Tax:

(1) Failure to File Return—In case of any failure to make and file a return or list, within the time prescribed by law, or prescribed by the

Commissioner or Collector in pursuance of law, the Commissioner shall add to the tax 25 per centum of its amount, except that when a return is filed after such time and it is shown that the failure to file it was due to reasonable cause and not to wilful neglect, no such addition shall be made to the tax . . ."

(b) The Regulations of the Treasury Department and the decisions of the Courts have established the basic proposition that:

"the delay is due to reasonable cause if the taxpayer exercised ordinary care and prudence."

(c) The Appellants in these cases contend that when, upon the death of their kin, they:

(1) Recognized their utter incapacity by reason of experience, training, education and background to discharge the manifold duties of the administration in probate of estates, including the task of preparing and filing complex federal tax returns, and

(2) Entrusted the performance of those duties to an attorney of outstanding reputation in their community whom they had known and relied upon for many years and was by reason of professional association familiar with the affairs of the deceased, and

(3) Did everything within their limited power to furnish their attorney with the tools and information required for the task, and responded to his every request for cooperation,

that they did everything that the law could expect of them as reasonable, prudent and conscientious individuals in the fulfillment of their obligations to the United States with respect to the filing of the federal estate tax return. Accordingly, they contend, the imposition of the penalties in question was illegal and erroneous, and that they ought to be refunded.

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2. ANALYSIS OF THE EVIDENCE.

(a) Wilful Neglect.

The Appellants in both these cases do not hesitate to say most emphatically that the finding of the Court below that the failure to file the return in question within the time prescribed by law was due to their wilful neglect is wholly unsupported by the evidence. This is not a question of insufficiency of the evidence —there is no evidence at all to support the finding.

(b) Reasonable Care and Prudence.

Estate of Ferrari.

1. Selection of Counsel.

At the time of their father's death, George and Edward Ferrari knew Lloyd Cosgrove not only as their father's attorney of many years standing, but as a well-known and reputable lawyer in their immediate community. Mr. Cosgrove had drawn the will of Mr. Ferrari and, quite naturally and promptly, after the death of their father, George and Edward turned to Mr. Cosgrove for his professional services required to settle the estate. Mr. Cosgrove accepted their em-

ployment and specifically undertook to do everything that was necessary to complete the administration of the estate, including the preparation and filing of such tax returns as may be required. (Tr. 113.) It is true that the Appellants did not inquire of Mr. Cosgrove as to whether he was an expert in matters relating to Federal Estate taxation, but the reason is plainly obvious. At that point they had no knowledge, nor had they ever had any occasion to become familiar with the laws or facts relating to Federal Estate taxes. They could not in the nature of things conceive of Federal Estate taxes as something separate and apart from the general administration of estates in probate, and thus exercise an independent judgment that some tax expert ought to be employed. That very decision itself had to be left to Mr. Cosgrove and he assumed the duty of making it.

2. Cooperation With and Assistance to Counsel.

As the probate file before the Court, and the testimony of the Appellants and Mr. Cosgrove, plainly indicate, Appellants responded to every request of Mr. Cosgrove for information and documents required by him in connection with the probate of the estate, made the necessary Court appearances, signed petitions and pleadings necessary, and consulted with him in his office on many occasions with respect to the various problems of administration of the estate.

3. Conduct of Appellants in Relation to Return.

With respect specifically to the federal estate tax return in question here, the testimony is clear and

uncontradicted that in the late fall of 1947 George and Edward Ferrari signed a federal estate tax return (which they referred to as federal estate tax papers) in the office of Mr. Cosgrove. This evidence has not been impeached or impugned in any way, and it is consistent with the testimony offered by Mr. George Ferrari in the criminal action involving Mr. Cosgrove in 1952 which counsel for the government quoted in this proceeding. (Tr. 181.) In the criminal proceeding, Mr. Edward Ferrari, as the government's own witness, testified that he signed the federal estate tax return and the preliminary notice "about the same time". The preliminary notice, as was stipulated in this proceeding, was filed in the Office of the Collector of Internal Revenue on December 2, 1947. To this must be added the Court's own conclusion in this case. (Tr. 27, No. 2.)

> "That *the return filed on December 2, 1947* . . . did not comply with the provisions of Section 821 . . ."

4. Mr. Cosgrove's Conduct in Relation to Return.

The substance of the testimony of Mr. Cosgrove with respect to the return was that he thereafter brought it to the office of Mr. Paul Doyle in an incomplete condition because of estimated valuations and lack of detail relating to liabilities, and at the time that the tax was paid in 1949 he went to Mr. Doyle's office, attempted to make certain corrections on this return, and then at the suggestion of Mr. Doyle took the return back to his office and retyped it. (Tr. 157.)

However improbable the latter testimony may be, there is no room to dispute the evidence in this case that a return was in fact signed by the Ferraris in the office of Mr. Cosgrove during the latter part of 1947. It is to be noted that the first sheet and the signature sheet of the federal estate tax return in evidence in this proceeding as Exhibit A bear a different serial number than the other sheets in the return, which indicates the signature page was signed at a time other than the time when the pages containing the detail with respect to assets and liabilities were inserted.

It is the unchallenged testimony of Appellants that they had no knowledge whatever of what transpired with respect to the return after the time they had signed it, except the representations that were made to them by Mr. Cosgrove on a number of occasions, as indicated in the testimony, that a return was in fact on file. These representations were made to the Ferraris by Mr. Cosgrove on three occasions:

First of all, when the Appellants asked Mr. Cosgrove if it was too late to change the valuations for Federal Estate tax purposes in the early part of 1948, at which time Mr. Cosgrove advised them that they could always make the change; (Tr. 183)

Second, when later in 1948 through Mr. DeMartini they learned of the requirements appearing on the face of Form 706 that "the tax is due 15 months after the date of the decedent's death", they went promptly to Mr. Cosgrove's office to inquire as to the status of the matter and were assured by him then that as long

as a return was on file, the (together with the statutory interest) tax could be paid as soon as the money was raised (Tr. 187); and

Finally, when this matter was raised again in 1949 after Mr. Baier, the attorney, had indicated to them the possibility of penalties being involved. (Tr. 189.)

5. Appellants Unaware a Complete Return Had Not Been Filed.

The relevance of the testimony of Mr. Cosgrove with reference to his relationship with the Office of the Collector of Internal Revenue in this proceeding was that there was no conduct on his part of which the Appellants could have been aware that would have put them on notice that the filing of the return had not been properly attended to, and that therefore some duty devolved upon them independently to see that some action was taken.

It is to be noted that, consistent with their understanding of the matter, the Appellants in this case, after arrangements had been made to borrow money to pay the tax, furnished Mr. Cosgrove not only with a check in payment of the tax reflected on the return, but a check in payment of the interest in full to the date of payment, both checks being dated as of the date of payment.

6. What More Was to Be Expected of Appellants?

It seems incomprehensive that any standard of reasonable care would then impose upon Appellants a personal duty to see that the return was filed in the office of the Collector of Internal Revenue any more than reasonable care would require that they see that

every other document involved in a probate proceeding was in fact filed with the proper official.

It seems grossly unreasonable to expect that the Appellants here should have been apprehensive that Mr. Cosgrove would not perform his duty in the filing of the return, when it appears that in fact he was performing his duties with respect to every other phase of the probate proceeding. It seems irrational to insist that executors of the experience and background of these Appellants should be asked to comprehend a different standard of obligation or duty or responsibility with respect to one phase of the probate of an estate than with regard to all other phases of the probate of an estate.

One might ask the question, "what should the Appellants have done here that they didn't do?" Should they personally have taken the return after it was signed to the Office of the Collector of Internal Revenue? Should they have gone to 100 McAllister Street, sought out the Estate Tax Division, independently inquired as to the law and regulations as respects the filing and payment of the tax, and to have checked the records from time to time to see that the return was filed or that extensions were duly obtained? Was there information required which they failed to furnish Mr. Cosgrove? Was there any action taken by them which prevented Mr. Cosgrove from doing his duty? Did anything occur within their knowledge that should have put them on notice that things were not right, from which a duty to take independent action would arise?

All these questions must be answered in the negative, and Appellants assert again that in good faith they did everything that could be expected of reasonable and prudent men to discharge their duty to the government in respect of this action.

Estate of Ferrando.

1. Background and Experience of Appellants.

Marguerite Ferrando, the widow of the deceased and a co-executor of his estate, was an elderly woman of little education. The testimony indicates that although she signed the various documents involved in the probate proceeding, and accompanied her son and co-executor, Fred Ferrando, to various meetings with their attorney, Mr. Cosgrove, she relied upon her son almost completely and discharged her duties under his direction.

Fred Ferrando grew up in the Mission District and did not himself complete high school. Upon finishing school he went to work in his father's concrete contracting business, and upon his father's death carried on the business.

In the conduct of this business he gained some familiarity with periodic tax returns of various types that are generally required to be filed in connection with the operation of a business and with respect to the income of individuals. He testified however that his income tax returns were prepared by accountants and that unemployment and withholding tax returns were prepared by a girl in his office and that his main responsibility was the payment of the tax itself. In

response to the question of government counsel that he was familiar with the fact that withholding taxes and unemployment taxes for the State were reported to the Franchise Tax Commission, he answered in the affirmative. This of course is not true, and inasmuch as there is no State withholding tax, and unemployment taxes are paid to the Department of Employment. (Tr. 41, 43.)

2. Selection of Counsel.

Mr. Ferrando testified that he had known Mr. Cosgrove for 18 years, and from time to time Mr. Cosgrove had represented him in various legal matters. He stated that Mr. Cosgrove had drawn his father's will and that, in the normal course of events, he turned to Mr. Cosgrove upon his father's death. He stated that he employed Mr. Cosgrove for the purpose of taking care of all matters required to be attended to in the course of the probate and administration of an estate.

3. Cooperation With and Assistance to Counsel.

Mrs. Ferrando testified that she knew of the excellent reputation of Lloyd Cosgrove in the community as an attorney, and that with her son she necessarily placed the burdens and responsibilities of administration of the estate in his hands. Mr. and Mrs. Ferrando testified, as did Mr. Cosgrove, that they complied with all of the requests of the latter for documents, and in due course and as they were asked, they signed the various petitions and affidavits required and made the necessary Court appearances.

4. Conduct in Relation to the Return.

With respect to the Federal Estate Tax, Mr. Ferrando testified that he received from Mr. Cosgrove a letter dated February 8, 1949 in which it was stated that the Federal Estate Tax return had been prepared, and asking that he and his mother call at the office for the purpose of signing it. The letter concluded, "Please give this matter your usual prompt attention". Mr. Ferrando testified that shortly after that time Mr. Cosgrove called and asked that Mr. Ferrando send him a check in the amount of $14,525.69 in payment of the tax disclosed on the return. He testified that the date appearing on the check, July 15, 1948, was not put on by him, but he does not recall the circumstances under which it was omitted at the time he made the check up.

Mr. Ferrando had no prior experience as an executor, and had never participated before this time in the probate of an estate. He had no independent knowledge as a layman as to the nature of these proceedings, including such things as Inventories and Appraisements, Inheritance Tax Affidavits, Estate Tax Returns, etc. There was no conceivable way in which he in his own mind could separate from the duties devolved upon Mr. Cosgrove one phase of the probate of the estate or another. He could not isolate the matter of the Federal Estate Tax return or the Inventory and Appraisement or the preparation of an Inheritance Tax Affidavit out of the whole fabric of the probate and reserve to himself special responsibility or devolve it upon someone else, because he had no comprehension of those things at all.

It is inconceivable that Mr. Ferrando, or any person with his background and experience, could have entertained a notion that the laws relating to Federal Estate taxes were something separate and apart from the general problems involved in the probate of an estate, which then placed special responsibility on him or required him to turn to someone other than his attorney.

5. There Was No Reason for Appellants to Distrust Mr. Cosgrove.

Examination of the testimony of Mr. Ferrando and Mr. Cosgrove, and a review of the file of the Superior Court, which was before this Court in this proceeding, negatives any suggestion or inference that Mr. Ferrando had any reason to doubt the competence of Mr. Cosgrove to handle all of the various phases of the probate administration, or that he was in any way neglecting his duties and responsibilities in the matter. There is also a striking absence of any fact or circumstance which might have served to bring to the attention of Mr. Ferrando any such feeling. The letter of February 8, 1949 is obviously routine in nature and, if any doubts were then in Mr. Ferrando's mind, could serve only to reassure him that matters were being attended to in the normal course of events.

It is of interest to note that at the time of the letter and at the time of the filing of the return in the Ferrando Estate, the time for the payment of the State Inheritance Tax (two years after the date of death), had not yet expired. Obviously it is not to be expected that a layman would, in his own mind, dis-

tinguish between the two unless it were specifically called to his attention.

Assuming, arguendo, that the apparent request of Mr. Cosgrove, or someone in his office, to Mr. Ferrando, to leave the check in payment of the tax undated should have aroused some suspicion in his mind at that time as to the status of the return, this event occurred a long time after the due date of the return had passed, and a substantial period of delinquency had expired.

The testimony of Mr. Ferrando and his mother on direct examination remained substantially unchallenged. It was not contradicted or impeached in any way whatsoever.

THE LAW OF THE CASE.

We have quoted the provision of the Internal Revenue Code involved in this proceeding on pages 11-12.

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1. MEANING OF TERMS.

There are no Treasury Department Regulations construing this Section of the Code, but Section 39.291-1 of Income Tax Regulations 118 states, with reference to similar language in the income tax law, that:

> "the delay is due to reasonable cause . . . if the taxpayer exercised ordinary care and prudence . . ."

With reference to the parallel provision of the income tax law (Section 291, Internal Revenue Code of 1939), the Supreme Court of the United States in *Spies v. United States,* 317 U.S. 492, 63 Supreme Court 364, has declared that:

> "It is not the purpose of the law to penalize frank difference of opinion or *innocent errors made despite the exercise of reasonable care.*" (Italics ours).

In an exhaustive review of the authorities on the subject, the Third Circuit Court of Appeals in a leading decision, *Hatfried, Inc. v. Commissioner of Internal Revenue,* 162 Fed. 2nd 628, concluded:

> "The Courts, as above stated, have ruled that 'reasonable cause means nothing more than the exercise of ordinary care and prudence' and 'willful' as 'intentional or knowing or voluntary'."

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2. RELIANCE ON COUNSEL.

In the *Hatfried* decision, supra, which involved a failure of an accountant for the taxpayer, upon whom he had relied, to file a personal holding company return, the Court said:

> "To hold that a taxpayer who selects as his agent a certified public accountant (to whom as a class the Treasury Department and The Tax Court itself accord recognition as 'experts' and as 'counsel') *has failed to exercise 'ordinary care and prudence' and becomes liable for the error of his advisor as 'agent' is an inconceivable proposition*" (Italics ours).

This remark and the one quoted above from the Court's opinion were made in answer to the broad contention of the government "that ignorance of the law is no excuse, whether that ignorance is on the part of the taxpayer or his advisor."

The leading case on the general subject involved here is the decision of the Second Circuit Court of Appeals in *Haywood Lumber & Mining Company v. Commissioner of Internal Revenue,* (1950) 178 Fed. 2nd 769. There, a corporation executive consulted a qualified certified public accountant and placed before him all necessary information about the affairs of the corporation which the accountant would require for the purpose of filing its return. The accountant admitted that he knew that the taxpayer was in fact a personal holding company, but through inadvertence failed to inform the officer of the corporation of this fact and to prepare the return in question. The executive was aware of the personal holding company statute, but had not studied its application and it did not occur to him that the corporation was in fact a personal holding company. The Tax Court sustained the imposition of the penalty but the Circuit Court of Appeals reversed. The Court pointed out that "reasonable cause" as used in the statute is defined in the Regulations (Section 39.291-1) to mean "that the taxpayer exercised ordinary business care and prudence". The Court of Appeals said:

> "When a corporate taxpayer selects a competent tax expert, supplies him with all the necessary information, and requests him to prepare proper tax returns, we think the taxpayer has

done all that ordinary business care and prudence can reasonably demand . . ."

"Respondent contends that where all the responsibility for the preparation of tax returns is delegated to an agent, the taxpayer should be held to accept its agent's efforts, cum onere, and be chargeable with his negligence . . . Further reflection convinces us that that proposition is not sound. The standard of care imposed by Section 291 is personal to the taxpayer. To impute to the taxpayer mistakes of his consultant would be to penalize him for consulting an expert; for he must take the benefit of his accountant's advice, cum onere, then *he must be held to a standard of care which is not his own and one which in most cases would be far higher than that exacted of a layman.*" (Italics ours).

We find no conceivable basis upon which these cases can be distinguished from the *Haywood* decision, though we do feel that the equities of these cases are stronger. The *Haywood* decision, for example, involved a corporation executive who had some familiarity with the statute involved and who, it is to be presumed, had a general knowledge of taxing statutes as a whole, so far as filing returns are concerned. Upon the facts, however, it is inconceivable that the same Court would view Messrs. Ferrando and Ferrari, for example, in a less favorable light.

The Treasury Department has now recognized the preponderance of authority which has followed the *Haywood* decision, and has accorded limited recognition to the principle enunciated. The Service will now excuse the late filing penalty in the cases of failure

to file personal holding company returns where there was reliance on the advice of tax counsel to the effect that no return was due. See *Revenue Ruling 172, 1953-2 CB 226.*

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3. FAILURE TO FILE AS DISTINGUISHED FROM ERRONEOUS ADVICE.

It is to be noted that the *Haywood* case, supra, involved mistake and inadvertence on the part of the taxpayer's counsel, who knew a return was in fact due. Thus, its application cannot be limited, as the Government would have it, to the erroneous exercise of judgment on the part of the adviser, but on the contrary applies as well to the consequences of the adviser's neglect or mistake.

This precise proposition has been affirmed by the Sixth Circuit Court of Appeals in *Fisk v. Commissioner of Internal Revenue,* 203 Fed. 2nd 358, a case involving the late filing of a Federal Estate Tax Return. In reversing the Tax Court, this Court said:

> "We think the addition of the penalty constituted error as a matter of law. The question of the existence of reasonable cause is in the first instance one for The Tax Court . . . which must decide whether the elements which constitute reasonable cause are present in the case. What elements must be presented to constitute reasonable cause is a question of law . . .
>
> "In *Hatfried, Inc. v. Commissioner,* supra, where it appeared that the only possible conclusion on the record was that the failure to file a personal holding company return was made on

an accountant's advice, the Third Circuit held that the finding that there was no reasonable cause was not sustained by substantial evidence. Whether we adopt the theory of this case or of the cases which *hold that in such matters reliance upon an attorney constitutes reasonable care as a matter of law,* the result is the same and the decision herein is erroneous . . .

"We adhere to the rules stated in *Haywood Lumber & Mining Co.,* supra, that as a matter of law reasonable cause was shown in this case. *This rule, we hold, applies to the filing of tax returns as well as to reliance upon technical advice in complicated legal matters.* We think this conclusion is in accord with the principle declared by the Supreme Court that the penalties under the revenue laws were designed to be imposed upon conduct 'which is intentional, or knowing, or voluntary, as distinguished from accidental' . . .

" 'It is not the purpose of the law to penalize . . . innocent errors made despite the exercise of reasonable care.' *Spies v. United States,* 317 U. S. 492 . . . "

The Tax Court recently followed this decision in an income tax case, *Lee Field, et al. v. Commissioner,* January 21, 1955, 14 T.C.M. (CCH Decision No. 2080 (M)). In that case the petitioners signed in blank a federal income tax return and left it with a public accountant with whom they had had previous business to prepare and file. The accountant, Mr. Eigen, completed the return in time for filing on the due date but, through inadvertence, placed it in the wrong file and it was not discovered until several

months later. Upon the authority of the *Estate of Kirchner,* 46 B.T.A. 578, and *Fisk v. Commissioner,* supra, the Tax Court concluded that the failure to file the return in time was due to reasonable cause and not to willful neglect.

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4. ESTATE TAX CASES.

The question here has been raised in a number of estate tax cases. Preliminarily, it should be pointed out that the filing of a federal estate tax return is a vastly different matter than filing a federal income tax return. To begin with, only a small fraction of estates subject to probate are required to file federal estate tax returns. In the second place, and of more significance, the responsible party in the case of estates very often becomes such solely by virtue of chance or by virtue of the relationship which he or she happens to occupy to the decedent. The vast majority of people are never in their lifetimes called upon to perform the duties of an executor, and to those upon whom the responsibility falls, it rarely happens more than once in a lifetime. As contrasted with this, the obligation to file federal income tax returns or ordinary sales tax returns or withholding returns, for example, might well be described as common knowledge, and it is an obligation which people in the ordinary course of affairs discharge many times in their lifetime.

The earliest decision on the precise question involved here is *Adelaide McColgan v. Commissioner,* 10

B.T.A. 959. This is a decision in which the Commissioner of Internal Revenue acquiesced. (VII-2 CB 26). In that case the Board of Tax Appeals said, with respect to the question of liability for the delinquency penalty:

> "Upon consideration of the evidence presented as to the third issue, we are of the opinion that the delinquency penalty for failure on the part of the petitioner to file an estate tax return within the time prescribed by law should not be asserted. Petitioner is a woman evidently unfamiliar with either the laws of California or the United States. She relied upon her attorney who advised her that under the circumstances the filing of an estate tax return for the decedent's estate was not required. She followed that advice . . . We think that under the circumstances the petitioner's failure to file an estate tax return on time was due to reasonable cause and not due to willful neglect and therefore the imposition of the penalty for such failure is not authorized."

In this estate, of course, the Appellants were completely unfamiliar with the laws of the State of California and of the United States relating to estates and inheritance taxation. They did, however, on many occasions discuss the progress of the estates in question with Mr. Cosgrove, the attorney in question, and repeatedly urged him to complete administration in every detail in order that the estates might be distributed as soon as possible. They did, in fact, do everything that was possible and could reasonably be expected of persons in their position to secure compliance not only with the laws of the United States but

with the laws of the State of California with respect to the administration of estates.

In the *Estate of Frederick C. Kirchner v. Commissioner,* 46 B.T.A. 758, which was decided 14 years later, there was involved an executrix, the widow of the deceased who, during the period of administration, "was not physically or mentally capable of looking after her business affairs. She was 65 years of age and had little or no knowledge of business affairs." Administration of the estate and the filing of tax returns was entrusted to a series of attorneys and an accountant who, for various reasons, failed to give proper attention to the matter of filing the tax returns. The Court held under the circumstances that the failure to file the return was due to reasonable cause, and that the Commissioner erred in imposing the penalty.

The Tax Court held similarly in 1950, in the case of the *Estate of Phillip S. Reichers,* 9 T.C.M. 403. The Court said:

> "The widow and her father were the executors of the decedent's estate. Neither had any experience as executors. The widow left all matters having to do with the estate to her father. He went to Levitt, a reputable, experienced attorney, and asked him to take care of everything in connection with the estate. Levitt assured him that he would do so."

It is true that The Tax Court has decided cases against the taxpayer on this question, but we are confident that this Court will readily observe the distinc-

tion between those decisions and the cases on which we rely. For example, in the *Estate of Curie,* 4 T.C. 1175, The Tax Court sustained the imposition of the penalty in a case in which the executor admittedly had full information necessary to file a return well within the time prescribed by law, and in addition had been warned by the Commissioner seven months and three months prior to the due date that the return must be filed in order to avoid the imposition of penalties. Obviously, on these facts there is no room for the contention that the failure to file was due to reasonable cause and, as a matter of fact, the Court suggested that willful neglect might be involved.

In *Estate of Abraham Werbalowski,* 9 T.C. 689, the Court, in sustaining the imposition of the penalty, distinguished the *McColgan* case upon the ground that the record did not show any clear understanding with the estate's attorney as to his responsibility so far as it covered federal estate tax matters, including the preparation and filing of the return. The evidence indicated that this responsibility devolved upon an accountant and it was also clear from the record that the executors personally undertook to discharge many of the chores required in the administration of the estate itself.

In *Estate of Arthur D. Cronin,* 7 T.C. 1403, the Court rejected the plea that where a failure to file a Federal Estate Tax return occurred because the attorney for the executor was not aware that there was any specific limit on the filing of the return was not attributable to reasonable cause. The Court said

that mere ignorance of the plain and unambiguous provisions of the statute and regulations prescribing the time for filing returns cannot be considered reasonable cause.

The decision in the *Cronin* case gives only cursory attention to the matter of the late filing of the return. It is not clear from the record what the exact circumstances of the case were. It is to be noted that three Tax Court judges dissented in the decision but it is not clear as to whether they dissented with respect to this issue or another issue which was in the case.

As pointed out above, the leading decision at the present time so far as estate tax returns are concerned is now the decision of the Sixth Circuit Court of Appeals in *Fiske v. Commissioner of Internal Revenue.* We feel that that decision is conclusive upon the issue presented in this case.

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5. DELAY IN PAYMENT OF TAX DISTINGUISHED.

These cases, of course, involve the payment of penalties expressly imposed in cases where there has been a failure to file a return on time without reasonable cause. The Internal Revenue Code of 1939 does not impose any penalty for the failure to pay estate or gift taxes within the time prescribed by law, although Section 145 of the Code does impose penalties for the failure to pay income taxes within the time prescribed by the law. The only statutory burden that must be met where estate taxes are paid late is the interest (6%) requirement.

It is also interesting to note that the Treasury Department Regulations 105 then in effect limits the Commissioner's authority to grant extensions of time for the filing of returns (Section 81.69) to three months, whereas in any case where the payment of the tax on the due date would impose undue hardship upon the estate, the Commissioner had authority to extend the time for payment for a "period or periods not to exceed in all ten years from the due date." (Section 81.79.)

These matters are pointed out especially with reference to the testimony in the Ferrari case that the Appellants here were made aware at the outset that delay in the payment of the tax would result in a 6% interest obligation, and that this obligation was met by them at the time of payment, and as of the date of payment. Thus, even though it be said that as a legal proposition, Appellants are foreclosed from pleading ignorance of the law, judgment for the government does not necessarily follow. For on the record, they acted in a manner consistent with the law; their error, if any, was reliance upon their attorney's representation of fact—that a return was in fact filed before the due date as extended.

CONCLUSION.

To state again the position of the Appellants in these actions, we feel strongly that the application of the principles of the decisions discussed above, which we are certain represent the weight of authority on

the question presented, will lead unerringly to the conclusion that when these Appellants consulted with Mr. Cosgrove, an attorney of long-established reputation, and whose confidence in him was based not only on that reputation but on the personal experience of their respective families over many years of time, and cooperated with him fully that they had "done all that ordinary business care and prudence can reasonably demand".

Dated, San Francisco, California,
January 21, 1957.

Respectfully submitted,
HENRY W. HOWARD,
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